

BEFORE THE  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554

In the Matter of

Implementation of the Pay Telephone Reclassification  
and Compensation Provisions of the  
Telecommunications Act of 1996

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CC Docket No. 96-128

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OFFICE OF THE SECRETARY

COMMENTS OF EXCEL COMMUNICATIONS, INC.

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## SUMMARY

This is the third time the Commission will attempt to devise a payphone compensation scheme pursuant to Section 276 of the Telecommunications Act. The first two payphone compensation plans were remanded by the United States Court of Appeals for the District of Columbia Circuit ("D.C. Circuit"). On this third attempt, the Commission should make every effort to devise a plan that would be consistent with the D.C. Circuit's repeated rulings. In both *Payphone I* and *Payphone II*, the D.C. Circuit clearly rejected the Commission's approaching of tying the rate for subscriber 800 and access code calls (hereinafter referred to jointly as "coinless calls") to the local coin rate.

Throughout this proceeding, the Commission has indicated a desire to promote competition among payphone service providers and to permit the market to set payphone rates. However, prescribing a market-based rate with a carrier pays system is problematic because no competitive market currently exists for coinless calls. As the Commission acknowledged, it had to base the coinless rate on the local coin rate, because it believed that was the best proxy for a market for coinless calls. Because of the lack of any discernible market, any "market-based rate" the Commission prescribes is highly likely to be arbitrary and capricious.

If the Commission wishes to adopt a market-based rate for coinless calls, it should adopt a calling party pays system. This option would assist the development of a competitive payphone market and would further the Commission's goals of promoting competition in the payphone industry. In addition, the calling party pays system would be much less burdensome to administer and regulate than a carrier pays system. A calling party pays system would also ensure that PSPs are paid on a regular and timely basis.

Moreover, the Commission's concerns regarding a calling party pays system are unfounded. First, the burden of depositing coins is not substantial because customers already associate a payphone with the need to deposit coins, especially since the vast majority of calls made from payphones are local coin calls. Second, because a calling party pays system would permit the use of a credit card or calling card to pay for access code calls, such a system would not violate TOCSIA.

If the Commission wants to prescribe compensation on a carrier pays basis, the rate must be tied to costs of originating coinless calls. In deriving a cost-based rate, the Commission must be certain to evaluate the costs of LECs as well as independent PSPs. Moreover, the IXC's have submitted data demonstrating that the cost of originating coinless calls is between \$.06 and \$.11. Even if the Commission averaged the results of the LEC and IXC data, the per-call rate would be approximately \$.13.

It is plain that the Commission must make substantial modifications to its approach to comply with the D.C. Circuit Orders and Section 276 of the Telecommunications Act. The Commission should recognize that although Section 276 requires *fair* compensation for calls originated at a payphone, fair compensation does not allow for PSPs to be overcompensated. The Commission's prior orders plainly overcompensate PSPs. Accordingly, the Commission should adopt a calling party pays system, or should adopt a rate based on the costs of originating payphone calls, which would at the most be \$.13.

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**COMMENTS OF EXCEL COMMUNICATIONS, INC.**

Excel Communications, Inc., on behalf of its operating subsidiaries, by undersigned counsel and pursuant to the Commission's Public Notice released June 19, 1998,<sup>1/</sup> hereby submits its Comments in the above-referenced proceeding.

**I. BACKGROUND**

Section 276 of the Telecommunications Act of 1996 directs the Commission to "establish a per call compensation plan to ensure that all payphone service providers are fairly compensated for each and every completed intrastate and interstate call using their payphone . . . ."<sup>2/</sup> This Public Notice represents the Commission's third attempt at devising such a compensation plan. On September 20, 1996, the Commission released its first Report and Order, in which the Commission determined that interexchange carriers ("IXCs") should compensate payphone service providers ("PSPs") directly, and set forth a three-phase process for such compensation.<sup>3/</sup> During

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<sup>1/</sup> Pleading Cycle Established for Comment on Remand Issues in the Payphone Proceeding, CC Docket No. 96-128 (June 19, 1998).

<sup>2/</sup> 47 U.S.C. § 276(b)(1)A).

<sup>3/</sup> In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, *Report and Order*, CC Docket No. 96-128 (rel. Sept. 20, 1996) ("Report and Order"), *Order on Reconsideration*, CC Docket No. 96-128 (rel. Nov. 8, 1996) ("Reconsideration Order").

the first year, the Commission established an interim compensation scheme, in which carriers would compensate PSPs on a flat-rate basis per-month. During the second year, the Commission reasoned that IXCs would be able to track and pay PSPs on a per-call basis. The Commission, therefore, determined that IXCs would compensate PSPs for each subscriber 800 call and access code call (hereinafter referred to jointly as "coinless calls") and set a default rate at \$.35. The Commission noted that \$.35 was the local coin rate in four of the five states that had deregulated their local calling rates and stated that "[i]f a rate is compensatory for local coin calls, then it is an appropriate compensation amount for other calls as well, because the cost of originating the various types of payphone calls are similar."<sup>4/</sup> During the third phase of payphone compensation, the individual payphone owners would set the rate for coinless calls.

Numerous parties appealed both the interim compensation plan and the default rate of \$.35. The United States Court of Appeals for the District of Columbia Circuit ("D.C. Circuit"), vacated and remanded both the interim compensation plan and the \$.35 default rate.<sup>5/</sup> In striking down the \$.35 default rate, the D.C. Circuit concluded that the Commission's decision was arbitrary and capricious because it tied the default rate to the local coin rate using the rationale that the costs of the two are similar, when the record was replete with evidence that the costs of coin and coinless calls are not similar. The Commission has not yet released an order revising its interim compensation plan.

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<sup>4/</sup> Report and Order, at ¶ 70.

<sup>5/</sup> *Illinois Public Telecom. Ass'n v. FCC*, 117 F.3d 555 (D.C. Cir. 1997) ("*Payphone I*").

Last fall, the Commission made another attempt at setting the default rate for coinless calls.<sup>6/</sup> This time, the Commission subtracted \$.066 per call from the starting rate of \$.35. The Commission reasoned that the \$.35 represents the "market" rate for coin calls and found \$.066 to be the difference between the cost of coinless and coin calls.<sup>7/</sup> Thus, the Commission concluded that the default rate would be \$.284. This rate was again struck down by the D.C. Circuit.<sup>8/</sup> In its Order remanding the \$.284 default rate, the Court reasoned

the Commission never explained why a market based rate for coinless calls could be derived by subtracting costs from a rate charged for coin calls. If costs and rates depend on different factors, as they sometimes do, then this procedure would resemble subtracting apples from oranges. If the Commission simply subtracted one quantity from another, logically independent quantity, its action was unreasoned.<sup>9/</sup>

In response to the Court's Order in *Payphone II*, the Commission has released this Public Notice. The Commission requests comments and evidence on various issues including: (1) whether the local coin rate reflects competitive market conditions and the extent to which costs and rates converge in the coin call market; (2) the similarities and differences between the market segments for coin and coinless calls and the factors attributable to these similarities and

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<sup>6/</sup> In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, *Second Report and Order*, CC Docket No. 96-128 (rel. Oct. 9, 1997) ("Remand Order").

<sup>7/</sup> Remand Order at ¶ 117.

<sup>8/</sup> *MCI Telecommunications Corporation, et al. v. Federal Communications Commission*, No. 97-1676, slip op. (D.C. Cir. May 15, 1998) ("*Payphone II*").

<sup>9/</sup> *Payphone II*, at 2.

differences; and (3) whether and how the distinctions between these market segments should affect the determination of a reasonable default compensation amount for coinless calls.

In view of the Court's now-repeated findings, Excel urges the Commission to cease its efforts to prescribe a so-called "market rate." While it is laudable that the Commission would prefer a rate for coinless calls that reflects a competitive environment, no such competitive environment exists and the Commission's attempt to create one will only lead to arbitrary and capricious rulemaking. Indeed, if the Commission wants to have a rate ruled by the market, it must allow the market to set the rate. A "calling party pays" instead of a carrier pays system would have this effect. By requiring the calling party to pay the cost for use of a particular payphone-- or to decline to do so-- the purchaser of the product (the end user) would also be the entity making the choice. This would permit a true market rate to develop. Absent a calling party pays system, the only rational method for prescribing a payphone rate would be to base the rate on the costs of providing the service.

## **II CALLING PARTY PAYS SYSTEM IS THE ONLY POSSIBLE MARKET-BASED COMPENSATION METHOD**

Throughout this proceeding, the Commission has indicated a desire to promote competition among payphone service providers and to permit the market to set payphone rates. In its first Report and Order the Commission stated that the "ultimate goal is to have a competitive payphone industry through rules and regulations that provide incentives to all the players in the industry to eliminate . . . the market distorting factors that exist today."<sup>10/</sup> Moreover, the Commission concluded that "the most appropriate way to ensure that PSPs receive compensation for each call,"

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<sup>10/</sup> Report and Order, at ¶ 8.



and to promote PSP competition "is to let the market set the price" for payphone calls.<sup>11/</sup> This preference for a market based coinless rate was also reflected in the Commission's Remand Order. The Commission stated, "[w]e conclude. . .that a market-based rate best responds to the competitive marketplace for payphones . . . ." <sup>12/</sup>

The problem with a market-based rate in a carrier pays system is that no competitive market currently exists for coinless calls. As the Commission acknowledged, it had to base the coinless rate on the local coin rate, because it believed that was the best proxy for a market for coinless calls. This reasoning is flawed. For instance, the markets for coin calls and coinless calls in a carrier pays environment are wholly different. In a coin call situation, the party paying the cost of the call is also the party making the economic decision as to whether to use the phone. In the current coinless call environment, the party paying for the use of the payphone (the IXC) has no ability to decide whether to even use the payphone to make the call. It is a third party, not directly bearing the economic burden, that makes the decision. In a carrier pays environment, therefore, the IXC has little if any leverage to negotiate price with the PSPs, because it is the IXC's customer that decides whether to use a payphone.

Because of the lack of any discernible market, any "market rate" the Commission prescribes is highly likely to be arbitrary and capricious. Absent an actual market, the process of trying to conjure a market in order to select a rate is fraught with arbitrary decisions and assumptions. Indeed, any rate that the Commission concludes is an appropriate market rate is

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<sup>11/</sup> Id., at ¶ 49.

<sup>12/</sup> Remand Order, at ¶ 24.

almost by definition arbitrary and capricious because a governmental agency is incapable of accurately predicting the forces of a competitive market in an area where none exists.

However, the Commission can base the rate for coinless calls on a competitive market by deciding to adopt a calling party pays system. This option would truly allow for a competitive market and would further the Commission's goals of promoting competition in the payphone industry. The calling party would have the incentive to "price shop" if the rate for subscriber 800 and access code calls at a particular phone were too high, which would consequently incent PSPs to compete with lower rates for such calls.

The calling party pays system has a number of other benefits in addition to its ability to help ensure a competitive rate for subscriber 800 and access code calls. The calling party pays system would be much less burdensome to administer and regulate than a carrier pays system. Currently, IXC's are burdened with substantial administrative costs in having to track and pay for each call originated at a payphone. The IXC's were required to devise a system for tracking payphone calls, wherein every quarter they must input ANI lists and invoice and pay every payphone owner for coinless calls. This requires IXC's to track billions of calls from over two million payphones and to compensate approximately 1500 payees. The carrier pays system also imposes administrative expenses on LEC's who must provide IXC's with quarterly lists of ANI's and must provide verification of disputed ANI's. As the Commission is fully aware, the tracking system and ANI coding systems are far from perfect. This year the Commission has been required to entertain and grant numerous waiver requests because of technical difficulties in passing through ANI coding digits. In addition, both the RBOC Coalition and APCC are

disputing amounts that various IXC's have paid. These disputes are certain to continue and increase administrative costs for all parties involved.

In contrast, the calling party pays system is virtually administration free and is an elegant yet simple solution that ensures payphone owners are timely paid. Instead of the IXC's having to track and pay compensation, the calling party simply (i) deposits coins into the payphone for subscriber 800 calls or (ii) has the option to either deposit coins or bill the amount to a calling card or credit card for access code calls. (Thus, as discussed in more detail below, under a calling party pays system the only calls that would require the actual deposit of coins would be subscriber 800 calls.) Pursuant to this compensation scheme, there is no additional administrative expense and payphone owners are paid immediately, in contrast to the current six month lag time. Moreover, there can be no dispute over how much money is owed, because the payphone owner will be assured payment by coins or direct billing every time the payphone is used. This will also alleviate the need for Commission resources in enforcement actions because of compensation disputes between IXC's and PSPs.

Moreover, the Commission's concerns regarding a calling party pays system are unfounded. The Commission concluded that any payment system that relies upon the deposit of coins would be unduly burdensome to transient payphone callers.<sup>13/</sup> However, customers already associate a payphone with the need to deposit coins, especially since the vast majority of calls made from payphones are local coin calls. It is, therefore, a logical extension to be required to deposit a coin for subscriber 800 and/or access code calls as well. Indeed, a calling party pays

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<sup>13/</sup> Report and Order, at ¶ 85.

system is more consumer oriented because it allows the customer to know up front the cost of the payphone call. Under the Commission's current system, the costs of the payphone call and the administrative costs are often hidden in increased rates for various services.

Although requiring consumers to deposit a coin to make a subscriber 800 call is not ideal, it is far more consumer oriented than requiring carriers to compensate PSPs at the unjustifiably high rates the Commission chose in its previous orders. As argued by the Consumer-Business Coalition in its Petition for Reconsideration,<sup>14/</sup> the high default rates set by the Commission will have a severely detrimental effect on businesses dependent on 800 service. For example, businesses such as airlines are particularly vulnerable to increased costs for using 800 services since many customers call airlines for numerous reasons from payphones. Moreover, the potential for fraud is greatly enhanced by a carrier pays system. As argued by the Coalition Petition, American Airlines calculated that continuous calls made from a single payphone to 800 numbers at one minute intervals would generate gross revenues of \$149,270 to the PSP annually. Coalition Petition, at 10. Such fraud, because it would most likely be dispersed among many IXC's, would be virtually impossible to detect. The current system could also have a detrimental effect on many public service hotlines such as those that assist runaways, drug addicts, and victims of domestic violence. According to the Coalition Petition, such services will not be able to afford the steep increase in 800 service costs and would likely have to block their 800 service from payphones. *Id.* at 14-15. Therefore, while it is not the ideal option to require a runaway or battered woman

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<sup>14/</sup> See The Consumer-Business Coalition for Fair Payphone 800 Fees, Petition for Reconsideration (submitted December 1, 1997) ("Coalition Petition").

to deposit a coin in a payphone to make a hotline call a calling party pays system will at least ensure that such hotlines are available from payphones.

Finally, TOCSIA does not prohibit a calling party pays system.<sup>15/</sup> As the Commission conceded in its Reconsideration Order, the prohibition in TOCSIA against advance payment by callers . . . "does not apply to subscriber 800 calls and therefore, is not dispositive. . . ." <sup>16/</sup> Carriers advocating calling party pays have stated all along that *only 800 calls would require the deposit of coins*. Customers would have the option of charging the call to their calling card or credit card for the access code calls that are governed by TOCSIA. Because customers have the option of paying later through their calling card or credit card, a calling party pays system would not require advance payments from consumers, and therefore, would not violate TOCSIA.

### **III. ANY PRESCRIBED RATE MUST BE BASED ON COSTS**

If the Commission wants to prescribe a rate for IXC's, the rate must be tied to costs. This theme is present throughout the D.C. Circuit opinions. In *Payphone I*, the Court noted that the Commission had erred in failing to consider the cost differences between coin and coinless calls.<sup>17/</sup> In *Payphone II*, the Court further expanded on the Commission's need to consider costs of originating coinless calls. The Court noted that the Commission failed to analyze whether "costs and rates do in fact converge in the coin call market."<sup>18/</sup> Indeed, although the Court stated that

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<sup>15/</sup> See 47 U.S.C. § 226(e)(2).

<sup>16/</sup> Reconsideration Order, at ¶ 89.

<sup>17/</sup> *Payphone I*, at 563.

<sup>18/</sup> *Payphone II*, at 2.

in principle, a market-based rate could satisfy the statutory requirement for fair compensation, "some explanation of the logic of the derivation of the market-based rate is still required."<sup>19/</sup>

Accordingly, the Commission could begin with the assumption that a competitive market would generally set a rate reflecting costs and would set a rate for coinless calls based on the costs of originating coinless calls. In determining the costs of originating coinless calls, the Commission must be certain to consider data that is representative of the entire payphone industry. In its Remand Order, the Commission made the mistake of solely relying on cost data provided by independent PSPs, although independents only operate about 20 to 25 percent of all payphones and typically have much higher costs than LEC PSPs.

LEC data already submitted in the record shows that costs for originating coinless calls, as submitted by the LECs is no higher than \$.16 to \$.18 per-call. For example, in the last round of comments, a number of parties submitted as evidence the proceeding in which NYNEX informed the Massachusetts DPU that its average per-call cost is \$.167.<sup>20/</sup> Because NYNEX was attempting to raise its rates in this proceeding, it had no incentive to understate its costs. In addition, in its Petition for Reconsideration, AT&T submitted data showing that the costs for Southwestern Bell ("SBC") payphones, after commission costs are removed, are approximately \$.162 per-call, which is very similar to the NYNEX data for Massachusetts. AT&T Petition for Reconsideration, at 15-16 (submitted December 1, 1997). In arriving at the per-call cost, AT&T

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<sup>19/</sup> *Id.* at 3.

<sup>20/</sup> See Comments of Sprint Corporation on Remand Issues, at 8-9 (submitted August 26, 1997) ("Sprint Comments"); Comments of AT&T ("AT&T Comments"), at 12-13 (submitted August 26, 1997); Comments of MCI ("MCI Comments") (submitted August 26, 1997), at 5.

first calculated a total average cost of \$93.11 per phone per month, which was derived by dividing SBC's total annual expenses, plus an additional amount representing the cost of access lines for semi-public phones, by SBC's total phone count, including semi-public phones. AT&T then applied the call count provided by the RBOC/GTE/SNET Coalition to get a cost per call of \$.195, including the cost of commission. Once commissions are removed the cost is \$.162.<sup>21/</sup> If the Commission decides to prescribe a rate based on costs, it must consider this LEC data, which is representative of 75-80% of PSPs.

Moreover, IXC's submitted data showing that the costs of originating coinless calls is even lower. For example, MCI submitted a study demonstrating that the per-call cost of completing access code calls from payphones, once coin-specific costs are eliminated, is approximately \$0.083. MCI Comments, at 3. AT&T also submitted data presenting an analysis of the costs it incurs for operating its own coinless phones. AT&T made some revisions to the data to reflect all of the costs PSPs even arguably incur to operate coinless phones, and modified the costs based on updated data. The result of the analysis was a per-call cost of approximately \$.11. AT&T Comments, at 11. Similarly, Sprint submitted data showing that per-call costs of coinless calls is approximately \$.06. Sprint Comments, at 11. Even if the Commission averaged the results of the LEC and IXC data, the per-call rate would be approximately \$.13.

Prescribing a coinless call rate based on actual costs for originating such calls is reasonable and avoids the faulty guesswork and assumptions inherent in attempting to set a "market rate." In addition, a cost-based rate that is significantly lower than the rates previously set by the

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<sup>21/</sup> *Id.* at 15.

Commission is in the public interest. As noted above, the Coalition's Petition detailed the harsh effects a high compensation rate could have on the businesses that use subscriber 800 numbers. Coalition Petition, at 15-17. Indeed, many businesses will be forced to block 800 numbers from payphones, which would certainly be contrary to the public interest and Commission intent. Accordingly, should the Commission decide to prescribe a rate, the rate should be based on the costs of originating coinless calls and should be set at no more than \$.13.

#### IV. CONCLUSION

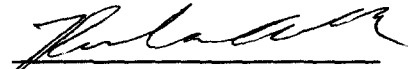
For the reasons stated above, Excel urges the Commission to abandon the idea that a governmental agency can prescribe a market rate for coinless calls based on the local coin rate. The markets are inherently different and attempting to base the rate for coinless calls on the local coin rate can only lead to arbitrary and capricious rulemaking. If the Commission wants the market to set the rate for subscriber 800 and access code calls, the Commission should adopt a calling party pays system. A calling party pays system would promote the Commission's objective in permitting the market to set payphone rates and would be less burdensome administratively than the current carrier pays system. However, if the Commission is intent on keeping the current carrier pays system, the rate must be based on the costs of originating coinless calls and should be no higher than \$.13. As explained above, the Commission should recognize that although Section 276 requires *fair* compensation for calls originated at a payphone, fair



compensation does not allow for PSPs to be overcompensated. The Commission's prior orders plainly overcompensate PSPs.

Respectfully submitted,

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Counsel for Excel Communications, Inc.

Dated: July 13, 1998


**CERTIFICATE OF SERVICE**

I hereby certify that, on this 13th day of July, 1998, two (2) copies of the Comments of Excel Communications, Inc. in the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996 (CC Docket No. 96-128) was hand delivered to:

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and one (1) copy of the Comments of Excel Communications, Inc. in the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996 (CC Docket No. 96-128) was hand delivered to:

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